

BEFORE THE
POSTAL RATE COMMISSION

RECEIVED

JUL 18 11 18 AM '00

POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

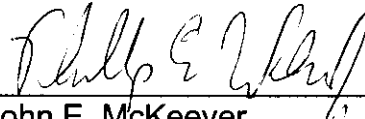
POSTAL RATE AND FEE CHANGES, 2000

DOCKET NO. R2000-1

ANSWERS OF UNITED PARCEL SERVICE WITNESS
DAVID E. M. SAPPINGTON TO INTERROGATORIES
OF THE UNITED STATES POSTAL SERVICE
(USPS/UPS-T6-53 through 55)
(July 18, 2000)

Pursuant to the Commission's Rules of Practice, United Parcel Service hereby files and serves the answers of UPS witness David E. M. Sappington to the following interrogatories of the United States Postal Service: USPS/UPS-T6-53 through 55.

Respectfully submitted,



John E. McKeever
William J. Pinamont
Phillip E. Wilson, Jr.
Attorneys for United Parcel Service

Piper Marbury Rudnick & Wolfe LLP
3400 Two Logan Square
18th & Arch Streets
Philadelphia, PA 19103-2762
(215) 656-3310
(215) 656-3301 (FAX)

and

1200 Nineteenth Street, NW
Washington, DC 20036-2430
(202) 861-3900

Of Counsel.

ANSWER OF UNITED PARCEL SERVICE WITNESS SAPPINGTON
TO INTERROGATORY OF THE UNITED STATES POSTAL SERVICE

USPS/UPS-T6-53. Please refer to your response to USPS/UPS-T6-42, part b., in which, based on a hypothetical that you present in your response to part a. of the same question, you decline to confirm that customers who are no longer purchasing a service (after a price increase) value the service or products that they consume instead more than they value the service that they have chosen to forgo.

a. Please confirm that when funds are received, they are available to be spent (with rare exceptions such as food stamps) however a person chooses, and are not limited *a priori* to be spent on particular categories of expenditures such as transportation, housing, or postage. If you do not confirm, please explain fully.

b. Please confirm that when the mailer in your hypothetical is postulated to have only \$10 to spend on postal services, it is because she has chosen to allocate her remaining funds to other uses based on her assessment of what those other uses are worth to her. If you do not confirm, please explain fully.

c. Please confirm that given a choice of spending \$10 for one postal service that meets her needs (Service A), or spending \$5 for a different postal service (Service B) that apparently also meets her needs, but to a more limited extent, **plus \$5 for whatever else she wants to buy**, she would only choose to spend the \$10 for Service A if the value to her of the Service A were more than the value to her of Service B, **plus** the value of whatever goods or services she can obtain with the remaining \$5. If you do not confirm, please explain fully.

d. Please confirm that given a choice of spending \$12 for one postal service that she was purchasing previously (Service A), or spending \$6 for a different postal service

ANSWER OF UNITED PARCEL SERVICE WITNESS SAPPINGTON
TO INTERROGATORY OF THE UNITED STATES POSTAL SERVICE

(Service B) **plus \$6 for whatever else she wants to buy**, she would only choose not to spend the \$12 for the original postal service if the value to her of the Service A were less than the value to her of Service B, **plus** the value of whatever goods or services she can obtain with the remaining \$6. If you do not confirm, please explain fully.

e. Given that the gross value of Services A and B remain constant regardless of the price, please confirm that the rationality of your hypothetical is contingent upon this particular mailer placing a disproportionate value on the alternative application of the sixth dollar of the \$6 difference between the new prices of Services A and B (relative to the value of the alternative application of the previous \$5 difference between the old prices of Services A and B). If you do not confirm, please explain fully.

f. Please confirm that any attempt to generalize your hypothetical, to explain why a subclass with a high own price elasticity is nevertheless one which customers value highly, would be dependent upon customers in general (or at least a substantial portion of them) placing the same disproportionate value on the alternative application of the new rate differential as does the particular individual mailer you have posited in your hypothetical. If you do not confirm, please explain fully.

Response to USPS/UPS-T6-53:

(a) Confirmed that individuals typically have discretion in how they allocate personal income that is not required to meet basic, essential needs. However, the same is not always true of departments or divisions in a business unit. Corporations often assign annual budgets to departments that limit spending on each of many

ANSWER OF UNITED PARCEL SERVICE WITNESS SAPPINGTON
TO INTERROGATORY OF THE UNITED STATES POSTAL SERVICE

different resources, such as travel, equipment, and mailing services. The head of the department or the person in charge of postal matters for the department in this setting might face the type of fixed budget for postal services that I describe in my response to USPS/UPS-T6-42.

(b) Confirmed that when a mailer has discretion to allocate funds across different uses, she will consider the value she derives from all such uses when deciding how to spend the funds. Notice, however, that in the setting described in my response to part (a), above, the person in charge of postal matters in the department of the corporation places little or no value on non-postal services, because she is not permitted to spend on other services funds that are designated for postal services.

(c) Confirmed, for the case of the individual (household) mailer that you have in mind. Note, however, that in the setting described in my response to part (a), above, the person in charge of postal matters in the department of the corporation does not have the opportunity to spend any unused portion of the budget for postal services on "whatever else she wants to buy."

(d) Confirmed, although please see the qualification discussed in my response to part (c), above.

(e) Although I am not certain of the exact meaning of the phrase "placing a disproportionate value on the alternative application of the sixth dollar of the \$6 difference between the new prices of Services A and B," I believe I can confirm that the spirit of your statement is correct. The essence of the example that I describe in my response to USPS/UPS-T6-42 is the following: The mailer finds it particularly onerous

ANSWER OF UNITED PARCEL SERVICE WITNESS SAPPINGTON
TO INTERROGATORY OF THE UNITED STATES POSTAL SERVICE

to increase her overall expenditures on postal services above some level. Such hardship can arise because the mailer truly has a fixed budget, for example (as in the setting described in my response to part (a), above). Alternatively, the hardship can arise because additional expenditures on postal services necessitate a reduction in expenditures on other highly valued commodities, such as essentials like food, clothing, and shelter. By switching to a less expensive (and less highly valued) postal service, the mailer secures additional funds that can be employed to purchase other essentials.

(f) Confirmed that the simple logic explained in my answer to part (e), above, would likely continue to underlie any generalization of the example described in my response to USPS/UPS-T6-42.

ANSWER OF UNITED PARCEL SERVICE WITNESS SAPPINGTON
TO INTERROGATORY OF THE UNITED STATES POSTAL SERVICE

USPS/UPS-T6-54. Please refer to the hypothetical presented in your response to USPS/UPS-T6-42, part a.

a. Please confirm that, in your hypothetical, the price of Services A and B both increase by 20 percent, the volume of Service A decreases, and the volume of Service B increases. If you do not confirm, please explain fully.

b. Please confirm that a necessary implication of your hypothetical is that, for this mailer, the cross-price elasticity of demand for Service B with respect to the price of Service A must exceed the own-price elasticity of demand for Service B. If you do not confirm, please explain fully.

Response to USPS/UPS-T6-54.

(a) Confirmed.

(b) Confirmed. Since the consumption of Service B increases while the consumption of Service A decreases when the price of Service A increases, the cross-price elasticity of demand for Service B with respect to the price of Service A is positive while the own-price elasticity of demand for Service A is negative. Therefore, the cross-price elasticity exceeds the own-price elasticity, as is always the case when the products in question are substitutes.

ANSWER OF UNITED PARCEL SERVICE WITNESS SAPPINGTON
TO INTERROGATORY OF THE UNITED STATES POSTAL SERVICE

USPS/UPS-T6-55. Please refer to the hypothetical presented in your response to USPS/UPS-T6-42, part a.

a. Please confirm that the context of the original question was to probe a portion of page 9 of your testimony in which you state that “a price increase may force customers with limited wealth to reduce their usage of a service substantially even though they cherish the service dearly.”

b. Please confirm that, in your hypothetical, the mailer has the option of using a premium postal service for \$10, or a slower service for \$5. If you do not confirm, please explain fully.

c. Please confirm that, in reality, when less expensive options are available, persons with “limited wealth” are unlikely to use a premium postal service, and are therefore unlikely to be in a position to “cherish [such a] service dearly.” If you do not confirm, please explain fully.

Response to USPS/UPS-T6-55.


(a) Confirmed.

(b) Confirmed.

(c) I can neither confirm nor refute your assertion, since I have not conducted a study of the spending habits of individuals with limited wealth.

DECLARATION

I, David E. M. Sappington, hereby declare under penalty of perjury that the foregoing answers are true and correct to the best of my knowledge, information, and belief.



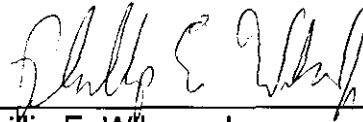
David E. M. Sappington

Dated:

7/18/00

CERTIFICATE OF SERVICE

I hereby certify that I have this date served the foregoing document by first class mail, postage prepaid, in accordance with Section 12 of the Commission's Rules of Practice.

A handwritten signature in cursive script, appearing to read "Phillip E. Wilson, Jr.", written over a horizontal line.

Phillip E. Wilson, Jr.
Attorney for United Parcel Service

Dated: July 18, 2000
Philadelphia, Pa.